



## A STRATEGY SPOTLIGHT

# Required Minimum Distribution Rules After the SECURE Act

A major benefit of tax-qualified retirement plans is the ability to accumulate savings on a tax-deferred basis (or tax-free, in the case of a Roth plan).

The Required Minimum Distribution (RMD) rules determine when the tax-advantaged accumulation must end. They detail when distributions must begin and how much must be distributed each year.

For IRA owners and many qualified retirement plan participants, the SECURE Act, signed into law on December 20, 2019, changed the starting year for these distributions from the year in which the taxpayer attains age 70½ to the year in which they turn age 72. Under the effective date provisions, the new rule applies to anyone who had not yet attained age 70½ by the end of 2019. The first RMD must be withdrawn by April 1st of the year after they reach the starting age of 72. This is referred to as the Required Beginning Date (RBD). For qualified plan participants who are working for the plan sponsor and do not own more than 5% of the plan sponsor, the first RMD can be delayed until April 1 of the later of the year in which they turn 72 or retire.

The SECURE Act ushered in much more dramatic changes to the complex rules that apply after the IRA owner or qualified plan participant's death. In this article, we'll cover these rules that generally apply to beneficiaries who inherit these types of accounts from an IRA owner or qualified plan participant who passes away after December 31, 2019.

On February 23, 2022, the Treasury Department released proposed regulations implementing the SECURE Act changes affecting RMDs from inherited IRAs and qualified retirement plans.

The changes made by the proposed regulations to the 10-year rule (detailed on the next page) apply to distributions required on or after January 1, 2023. No penalties will be assessed for annual RMDs under the 10-year Rule that were not taken in 2021 and 2022. (IRS Notice 2022-53). You should consult your tax advisor for further guidance.

To better understand the required distribution rules that apply to a specific beneficiary we must look at the three categories of beneficiaries under the SECURE Act.

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### 1 | Designated Beneficiary

- Individual.
- See-through trust.

### 2 | Eligible Designated Beneficiary— Designated beneficiary who is either:

- A surviving spouse.
- The child of deceased who has not yet reached age of majority.
- Not more than 10 years younger than the deceased.
- Chronically ill.
- Disabled.

### 3 | No Designated Beneficiary

- Estate.
  - Non-qualifying trust.
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## 1. Designated Beneficiary

This is a beneficiary of an IRA or qualified retirement plan that is an individual or what is often referred to as a “see-through trust,” which is generally an irrevocable trust where all of the trust beneficiaries are individuals.

Prior to the SECURE Act, a designated beneficiary was required to take minimum distributions from the inherited account each year that were calculated using their life expectancy or, in certain situations, the life expectancy of the deceased if it was longer.

The SECURE Act imposes a new 10-year rule for a designated beneficiary. The application of this rule depends upon whether the traditional IRA owner or qualified plan participant died before their Required Beginning Date (RBD) as discussed above, or on or after their RBD. If they died **before** their RBD, all of the inherited funds must be distributed by December 31st of the year that contains the 10th anniversary of their death, and there are no periodic distributions required. This application of the 10-year rule also applies to the designated beneficiary of a Roth IRA. If the traditional IRA owner or qualified plan participant died **on or after** their RBD, the proposed regulations provide that designated beneficiary must take annual RMDs beginning in the year after death (no penalties assessed for missed distributions in 2021 and 2022), and the inherited account must be fully liquidated by December 31st of the year that contains the 10th anniversary of their death. The RMDs for years 1 – 9 are based on the life expectancy of the beneficiary (or traditional IRA owner/plan participant, if longer). Designated beneficiaries of Roth 401(k) accounts are subject to this 10-year rule if the participant died after their RBD.

## 2. Eligible Designated Beneficiary

These are designated beneficiaries of an IRA or qualified retirement plan that are eligible to take annual required distributions (beginning in the year after death) of the inherited funds over their life expectancy (modified version for minor child), or the life expectancy of the deceased, if longer. To determine the distribution period, they use the factor from the Single Life Table for the age they attain in the year after the death of the IRA owner or qualified retirement plan participant.

An eligible designated beneficiary of a Roth IRA, or traditional IRA or qualified retirement plan where death occurred before the RBD, may instead elect to follow the 10-year rule for deaths before RBD.

## Surviving Spouse

The surviving spouse has a choice: elect a “spousal rollover” or treat the account as an inherited account:

- **Spousal rollover.** Most often it will be in their best interest to elect a “spousal rollover,” which allows them to transfer the inherited account balance to their own IRA or qualified retirement plan. There is no time limit on their ability to execute a spousal rollover.
- **Treat as an inherited account.** If the surviving spouse is under the age of 59½, distributions from their own IRA or qualified retirement plan will be subject to the 10% penalty. They may consider waiting until they attain that age to execute the rollover. This allows them to take withdrawals from the inherited account, if needed, without incurring the 10% early distribution penalty.

Distributions from the inherited account are not required until the later of:

- The year following the year of the IRA owner or qualified retirement plan participant’s death.
- The year in which the IRA owner or qualified retirement plan participant would have attained age 72, if they died on or after 1/1/2020.
- The year in which the IRA owner or qualified retirement plan participant would have turned age 70½, if they were born before 7/1/1949 and died before 1/1/2020.

This delayed RMD starting date gives younger surviving spouses the flexibility of taking penalty-free withdrawals from the account only if needed.

When distributions are required, the surviving spouse would use the Single Life Table to determine their life expectancy factor. Unlike a non-spouse beneficiary, the life expectancy of the surviving spouse beneficiary is recalculated annually, which means they return to the Table each year and use the factor associated with their attained age.

A younger surviving spouse can execute a spousal rollover sometime after attaining age 59½, so that RMDs are calculated using the more favorable Uniform Lifetime Table (found in IRS Publication 590-B) resulting in smaller RMDs.

The surviving spouse has another option if the deceased spouse dies before they are required to withdraw their first RMD (generally April 1st of the year after attaining age 72 for those born after June 30, 1949). They can elect to follow the 10-year rule described previously. This option is rarely chosen by the surviving spouse unless their life expectancy under the applicable table is less than 10 years.

## Minor Child

The minor child of the IRA owner or qualified retirement plan participant who has not reached the age of majority, as of the date of the IRA owner or plan participant's death, follows the life expectancy payout method until they reach majority. The regulations provide that a child reaches the age of majority on their 21st birthday. In the year after they reach age 21, they must switch over to the applicable 10-year rule discussed previously. The inherited account must be fully liquidated by December 31st of the year in which they attain age 31.

## Disabled Person

The life expectancy payout method also applies to an individual beneficiary who is disabled, as well as a trust in which the disabled person is the sole life beneficiary of the trust.

A disabled person, age 18 or over, is treated as an eligible designated beneficiary if they are unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or to be of long continued and indefinite duration.

Those under the age of 18 must have a medically determinable physical or mental impairment that results in marked and severe functional limitations and that can be expected to result in death or to be of long continued and indefinite duration.

If, as of the date of the IRA owner or qualified retirement plan participant's death, the beneficiary qualifies for Social Security disability benefits, they will be deemed disabled for purposes of qualifying as an eligible designated beneficiary.

The individual must provide proof of their disability to the IRA custodian or qualified retirement plan administrator by October 31st of the year after the IRA owner or qualified retirement plan participant's death.

## Chronically Ill Person

The life expectancy payout method also applies to an individual beneficiary who is chronically ill, as well as a trust in which the chronically ill individual is the sole life beneficiary of the trust.

A chronically ill person is treated as an eligible designated beneficiary if they have been certified by a licensed health care practitioner as:

- Being unable to perform at least two activities of daily living for a period of at least 90 days due to loss of functional capacity or having a similar level of disability.
- Requiring substantial supervision to protect such individual from threats to health and safety due to cognitive impairment.

**The individual must provide documentation of their chronic illness that includes a certification by a licensed health care practitioner to the IRA custodian or qualified retirement plan administrator by October 31st of the year after the IRA owner or qualified retirement plan participant's death.**

## Beneficiary That is Not More Than 10 Years Younger

An individual beneficiary who is not more than 10 years younger than the deceased IRA owner or qualified retirement plan participant (using dates of birth) is an eligible designated beneficiary and, as such, will follow the life expectancy payout method.

## 3. No Designated Beneficiary

On occasion an IRA owner or qualified retirement plan participant will name their estate as the beneficiary of their account. Or, in the event they die without having named a beneficiary, generally their estate will be the default beneficiary. An estate is not a designated beneficiary for RMD purposes, so the post-death RMD rules described above do not apply. Another entity that does not follow the distribution rules for a designated beneficiary is a trust if one or more of the trust beneficiaries are not individuals.

The applicable distribution rules for the beneficiary that is not a designated beneficiary depend upon whether the IRA owner or qualified retirement plan participant died before or after April 1st of the year after the year in which their first RMD was determined. For those born after June 30, 1949, this is generally the April 1st of the year after attaining age 72. This date is referred to as the Required Beginning Date (RBD).

- **Death before RBD:** All inherited funds must be distributed by December 31st of the year that contains the 5th anniversary of the date of death, and during that period there are no periodic distributions required.
- **Death after RBD:** The inherited funds must be distributed “at least as rapidly” as the method of distribution applicable during the owner’s lifetime. Generally, this means that the funds must be distributed over a period of time that is equal to the deceased IRA owner or qualified retirement plan participant’s remaining life expectancy under the Single Life Table.

The post-death RMD rules are complex. To best accomplish certain planning goals in regards to these assets that will be inherited by your heirs, you should work with your personal tax and legal advisors to discuss our specific situation.

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**Note:** This Strategy Spotlight covers the highlights of the new rules and is not intended to be a comprehensive review of the changes. A particular product or plan may not offer all of the options that are allowable under the law.

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